No. 09-981

Supreme Court, U.S.
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Supreme Court of the United States

JOHNSON CONTROLS, INC.; SECURITY GROUP, INC. AND SUBSIDIARIES, INCLUDING SARGENT & GREENLEAF, INC.; WILLIS NORTH AMERICA, INC. AND AFFILIATES; BUNZL USA, INC.; TREDEGAR CORPORATION, INC. AND SUBSIDIARIES; RAYCOM TV BROADCASTING, INC., AS SUCCESSOR-IN-INTEREST OF COSMOS BROADCASTING CORPORATION AND AFFILIATES, PETITIONERS
Petitioners,

v.

JONATHAN MILLER, SECRETARY OF THE FINANCE AND ADMINISTRATION CABINET OF THE COMMONWEALTH OF KENTUCKY; COMMONWEALTH OF KENTUCKY, DEPARTMENT OF REVENUE
Respondent.

On Petition For A Writ of Certiorari to the Supreme Court of Kentucky

BRIEF OF *AMICUS CURIAE* COUNCIL ON STATE TAXATION IN SUPPORT OF PETITIONERS

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INTEREST OF *AMICUS CURIAE*

The Council On State Taxation ("COST") is a non-profit trade association formed in 1969 to promote equitable and nondiscriminatory state and local taxation of multi-jurisdictional business entities. COST represents nearly 600 of the largest multistate businesses in the United States; companies from every industry doing business in every state.[1] As amicus, COST has participated in many of this Court's significant cases over the past 20 years involving remedies and retroactive state taxes, including *Newsweek, Inc. v. Florida Dept. of Rev.*, 522 U.S. 442 (1998); *Reich v. Collins*, 513 U.S. 106 (1994); *McKesson Corp. v. Division of Alcoholic Beverages and Tobacco*, 496 U.S. 18 (1990).

Many of COST's members are engaged in business in the Commonwealth of Kentucky, and thus have a particular interest in fair and equitable taxation in Kentucky. COST's primary concern with this case is the significant Due Process issues raised by this case. Given the states' current budget deficits, the issue of states retroactively taking away taxpayers' rights to a refund of tax is of national concern. Other states have passed legislation with retroactive periods significantly longer than those ever condoned by prior holdings of this Court, and guidance from this Court would prevent other states from trampling upon

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[1] No counsel for a party authored this brief in whole or in part, and no counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than *amicus curiae*, its members, or its counsel made a monetary contribution to its preparation or submission. The parties received timely notice of COST's intent to file this brief. Petitioner and Respondent have each consented to the filing of this brief.

taxpayers' Due Process rights with similar retroactive legislation. Moreover, attempts by States to deprive taxpayers of adequate remedies to challenge unlawful taxes leaves taxpayers in a position where compliance with tax laws is discouraged, since they are never assured that they will have a method contest their tax liabilities.

COST members are also weary, if Kentucky's deprivation of judicial remedies is permitted to stand, that more states will follow suit; induce taxpayers to pay disputed taxes, and then once paid, leave taxpayers with no remedy to dispute the liability. Undoubtedly, numerous states would be inclined to follow this model set forth by Kentucky because then states can impose unlawful taxes with no concern to provide a judicial remedy guaranteed by the Constitution and Fourteenth Amendment. In addition, other states already have and will continue to impose tax legislation with lengthy and excessive retroactive periods that violate taxpayers' Due Process rights. This is not only unjust but runs afoul of the principles of a fiscally sound tax system that heavily relies on voluntary compliance. Taxpayers' are less likely to voluntarily comply with tax laws perceived as unfair.

STATEMENT OF THE CASE

This case involves Petitioners' detrimental reliance on a claim for refund statute in existence at the time they filed amended returns, and then subsequently abolished after the taxpayers filed their amended returns, leaving them no judicial remedy to challenge their dispute taxes. In 1988, the Kentucky Department of Revenue's policy required all corporate taxpayers to file a "separate" income tax return for each company. That policy was success-

fully challenged in 1994 as being inconsistent with Ky. Rev. Stat. §141.120, and the Kentucky Supreme Court held that certain taxpayers could file a "combined" income tax return that included all related companies. *GTE and Subsidiaries v. Revenue Cabinet*, 889 S.W. 2d 788, 793 (Ky. 1994).

Petitioners and 23 other taxpayers amended their Kentucky tax returns for the tax years still open for refund, tax years 1990-1994. The refunds were filed on a combined basis consistent with *GTE*. When the amended returns were filed, Ky. Rev. Stat. §141.200 provided a post-deprivation remedy by means of filing a claim for refund. Subsequently, several years later in 2000, the Kentucky legislature amended Ky. Rev. Stat. §141.200 to deprive petitioners of their right to a claim for refund for any taxable year on or before December 31, 1995. That legislation left those taxpayers with no avenue to dispute their tax liabilities arising from the amended returns.

SUMMARY OF THE ARGUMENT

"Nothing in life is certain," but the Constitution embodies language designed to make some things less uncertain. The Fourteenth Amendment guarantees a minimum level of "due process." The Due Process Clause embodies guiding principles for conduct of the States with respect to those over whom they exercise jurisdiction, including the principles of certainty, fairness, balancing of interests (the State's and the individual's), and respect for property rights. All four of these principles are implicated by the structure and operation of a State's taxation and remedial schemes.

This case presents the clearest evidence that when a state is faced with fiscally grounded arguments against providing relief, many State courts will disregard the basic tenets of Due Process in order to avoid paying refunds to a taxpayer who has *successfully* challenged a state tax. The Kentucky Supreme Court's response to the taxpayers in this case is violative of Due Process in two ways. First, Kentucky's legislation at issue in this case has a retroactive period of six to ten years—a period significantly longer than those permitted in prior cases by this Court. This is a growing trend among states, and their justification for enacting such retroactive legislation—raising or preventing erosion of revenues—is very different from this Court's initial use of such justification to permit legislation with a retroactive period of 1-2 years as utilized by customary congressional practice.

Kentucky has twisted this justification such that it could enact retroactive legislation looking back decades. The result is that the rational legislative purpose test proclaimed by this Court no longer places any restrictions on states with respect to retroactive tax legislation, and synonymously, does away with taxpayers' Due Process rights.

Secondly, Kentucky's use of the bait-and-switch tactic previously rejected in *McKesson Corp. v. Florida* has eviscerated any remedy petitioners and other taxpayers have to dispute their tax liability for tax years 1990-1994. That deprivation of the only remedy taxpayers had results in the payment of taxes without a "clear and certain remedy." *McKesson Corp. v. Florida*, 496 U.S. 18, 39 (1990). By denying the applicability of the post-deprivation refund statute to taxes later found to be improper, the Kentucky

Supreme Court tilts the scales balancing State and taxpayer interests completely in the States' favor and depriving taxpayers of the "clear and certain" remedy to which they are entitled under Due Process. This Court needs to correct the interpretation of state taxation schemes by state courts where such courts either consciously disregard or purport insincerely to apply Due Process principles in such a way as to achieve a predetermined result, *i.e.*, the denial of refunds to taxpayers who have been subject to an unconstitutional tax.

ARGUMENT

I. THIS COURT SHOULD PROVIDE GUIDANCE AS TO A CONSTITUTIONALLY-PERMISSIBLE LENGTH OF RETROACTIVITY FOR TAX LEGISLATION THAT IS CONSISTENT WITH TAXPAYERS' DUE PROCESS RIGHTS

States frequently turn to retroactive tax legislation as a way to mend their budget gaps by changing the law for prior tax periods. Sometimes the retroactive period is modest, but often the retroactive period is extended—like the six to ten years at issue here. Legislation altering the rules for such a long period are not justified by the mere need to raise revenues. If upheld, the retroactive legislation effectively eviscerates the rational legislative purpose test previously announced by this Court for determining whether the period of retroactivity violate Due Process.

This Court last addressed retroactive tax legislation in *U.S. v. Carlton* in 1994, when the Court reiterated the test used in *Pension Benefit Guaranty* to uphold a statute with a 5 month retroactive period:

"But that burden is met simply by showing that the retroactive application of the legislation is itself justified by a rational legislative purpose." *Pension Benefit Guaranty Corp. v. R.A. Gray & Co.*, 467 U.S. 717, 730 (1994). The case at hand illustrates the need for guidance by this Court because the Kentucky Supreme Court's application of the rational legislative purpose test differs greatly from how this Court initially applied this test in *Carlton*. *Carlton* addressed situations where legitimate reasons may exist for imposing a short retroactive period that was the result of a customary legislative process. The cases decided by this Court upholding retroactive tax legislation are distinguishable from this case in two significant ways: (1) the rational legislative purposes for permitting the retroactive tax legislation and (2) the length of applicable retroactivity.

A. The Rational Legislative Purposes Approved by this Court Do Not Justify Depriving Taxpayers of their Post-Deprivation Judicial Remedy After They Relied on It To File Amended Returns.

The legislative purposes previously accepted by this Court to justify the enactment of retroactive tax legislation differ from the purposes accepted by the Kentucky Court in two distinct ways. First, in many of the Court's cases the retroactive legislation would have been far less effective in accomplishing its goals if had not been enacted with a *short* retroactive period. Second, in other cases, the legislatures were merely altering tax burdens—rather than completely depriving taxpayers of their right to a post-deprivation remedy. Thus, although the Court has upheld raising revenues as a rational legislative pur-

pose in a few cases, those cases are clearly distinguishable. Those decisions do not completely deprive a taxpayer of a post-payment remedy that the taxpayer justifiably relied on to dispute its tax liability.

(i) In Previous Cases This Court Has Upheld Retroactive Tax Legislation When There Existed a Justifiable Reason For Having a Short and Limited Retroactive Period.

In *Pension Benefit Guaranty*, this Court identified Congress' rational legislative purpose as a concern that once employers got wind that Congress was considering legislation that would sharply increase tax liability for those withdrawing from multi-employer pension plans, employers would take drastic action prior to the effective date of the legislation. *Pension Benefit Guaranty Corp v. R.A. Gray & Co.*, 467 U.S. 717, 730-31 (1984). "Congress therefore utilized retroactive application of the statute to prevent employers from taking advantage of a lengthy legislative process and withdrawing while Congress debated necessary revisions in the statute." *Id.* at 731. To be sure, the legislation would have been entirely ineffective if employers rushed to withdraw without liability before the legislation was enacted.

In comparison, petitioners in this case were retroactively deprived of their ability to dispute their tax liabilities. There was never a legitimate concern about the effectiveness of legislation, rather the legislature specifically targeted petitioners to deny them a constitutionally guaranteed judicial remedy that was available to all other taxpayers. Increasing a pension plan's withdrawal liability for a short retroactive period stands in stark contrast to the stripping a group of taxpayers of their right to contest their tax liabilities.

(ii) Raising Revenue as a Rational Legislative Purpose Should Not Be Allowed to Justify Every Retroactive Tax Change.

In *U.S. v. Carlton*, this Court stated: ". . . Congress' purpose in enacting the amendment was neither illegitimate nor arbitrary. Congress acted to correct what it reasonably viewed as a mistake in the original 1986 provision that would have created a significant and unanticipated revenue loss." 512 U.S. 26, 32 (1994). While this Court in *Carlton* accepted revenue preservation as a rational legislative purpose, the rationale was never intended to justify the unlimited retroactive enactment of tax legislation. Virtually all retroactive tax legislation increases or protects revenues. Consequently, limits on retroactivity would never apply.

In *Carlton*, the legislation at issue was IRC §2057, which allowed estates a "deduction for half the proceeds of 'any sale of employer securities by the executor of an estate' to 'an employee stock ownership plan.'" 512 U.S. 26, 28 (1994) (citing §2057(b)). The retroactive amendment limited the deduction to a certain group of decedents—those who owned the stock immediately before their death because otherwise, "taxpayers could qualify for the deductions by engaging in essentially sham transactions." *Id.* at 32. This led the Court to allow the "curative" amendment with a short retroactive period, in order to implement the legislation as Congress had originally planned.

In stark contrast to the curative amendment in *Carlton*, here there was no initial legislation that the state legislature was attempting to fix to avoid taxpayers from engaging in "sham transactions." Rather, the state legislature acted purposely and aggressively to deny taxpayers their right to dispute

their tax liability, leaving them with no legal remedy for challenging their tax liabilities. The retroactive denial of a statutory judicial remedy for a small and specific group of taxpayers, that has long existed for all other taxpayers in the jurisdiction can hardly be justified as preserving revenues since all the taxpayers desired was their day in court to challenge the accuracy of their tax liabilities.

B. The Length of Retroactivity Previously Permitted by this Court is Distinguishable from the Lengthy Six to Ten Years Faced by Petitioners.

What this Court referred to as a "modest period of retroactivity" in *U.S. v. Carlton* should be reiterated and refined in order to remove the temptation from states to enact retroactive tax legislation far beyond what this court likely imagined as "modest" when *U.S. v. Carlton* was decided. States have enacted retroactive legislation under the guise of losing revenues for retroactive periods extending many years beyond the retroactive periods previously permitted by this court and encompassed by the time necessary for customary congressional practice.

Nothing in this Court's prior jurisprudence suggests that retroactive tax legislation could reach back six to ten years as was done so here by Kentucky. In *U.S. v. Carlton*, this Court upheld an amendment that "extended for a period of slightly greater than one year." 512 U.S. 26, 33 (1994). In *Pension Benefit Guaranty*, this Court upheld retroactive tax legislation reaching back "five months before the statute was enacted into law." *Pension Benefit Guaranty*, 467 U.S. 717, 725 (1984). In *Welch v. Henry*, this Court upheld an amendment enacted in 1935 reaching back to the 1933 tax year. *Welch v. Henry*,

305 U.S. 134, 141-42 (1938). These modest periods of retroactivity are far shorter than Kentucky's six to ten year grasp.

The lower court decisions cited by the Kentucky Supreme Court in order to justify the length of the retroactive period highlights the need for this Court to provide clear guidance for lower the courts to follow when reviewing periods of retroactivity. Without such guidance, there will be inconsistent decisions by the lower courts and some courts will continue to bless lengthy retroactive periods that violate taxpayers' Due Process rights.

This Court has allowed short and modest periods of retroactive tax legislation with the underlying concern and recognition for the practicalities of the legislative process. *See, e.g., Untermyer v. Anderson*, 276 U.S. 440 (1928); *United States v. Darusmont*, 449 U.S. 292 (1981); and *Welch v. Henry*, 305 U.S. 134 (1938). Specifically this Court has permitted short retroactive legislation based on the premise that customary congressional practice is to pass legislation "to tax retroactively income or profits received during the year of the session in which the taxing statute is enacted, and in some instances during the year of the preceding session." *Welch v. Henry*, 305 U.S. 134, 148 (1938). This Court noted numerous instances of legislation that was made retroactive for the year prior to the passing of the legislation in *Untermyer v. Anderson*, and stated, "I suppose that the taxing act may be passed in the middle as lawfully as at the beginning of the year." 276 U.S. 440, 446 (1928) (Sanford and Holmes J., concurring).

The "practicalities" of producing legislation should in no way justify the six to ten year retroactive period here. While the Kentucky Supreme Court found that

the lower court relied too heavily on Justice O'Conner's concurring opinion that stated the retroactivity period should not exceed one year, it also noted the important language from the majority opinion in that case: "This 'customary congressional practice' generally has been confined to short and limited periods required by the practicalities of producing national legislation." Slip op. at 33. If this Court allows a six to ten year retroactive period to satisfy a modest period of retroactivity, legislatures will merely continue to expand the length of retroactivity and offer excuses to justify their inability to enact legislation sooner.

II. KENTUCKY'S DEPRIVATION OF MEANINGFUL BACKWARD LOOKING RELIEF FOR TAXPAYERS WHO PAID DISPUTED TAXES VIOLATES THE DUE PROCESS CLAUSE BY DENYING TAXPAYERS ALL REMEDIES FOR DISPUTING THEIR TAX LIABILITIES.

Due Process requires that states provide a "'clear and certain remedy' for the State's unlawful exaction of tax moneys under duress." *McKesson Corp. v. Florida*, 496 U.S. 18, 33 (1990). That remedy can be offered by the state pre-payment or post-payment of the taxes, but what has been reiterated by this Court numerous times is that a state cannot induce a taxpayer to rely on a post-payment remedy only to deprive him of that remedy once the taxpayer has paid the disputed taxes and files a claim for refund. *Reich v. Collins*, 513 U.S. 106, 110-11 (1994). What has occurred in this case mirrors the same scenario as *Reich v. Collins*. The Kentucky Petitioners relied on the availability of post-deprivation relief provided by the earlier version of Ky. Rev. Stat. §141.200, paid

their disputed taxes in reliance on that judicial remedy, and then subsequently were deprived of that remedy when they filed suit to dispute their tax liabilities.

In *McKesson Corp. v. Florida*, this Court imposed a requirement that states not deprive taxpayers of meaningful backward-looking relief when they require a taxpayer to pay first and litigate later. 496 U.S. 18, 31 (1990). The Court should clarify that this remedy is unconditional regardless of which law the tax violates because the availability of a judicial remedy to dispute taxes previously paid is fundamental to a fair and efficient tax system.

The cases mentioned by this Court in *McKesson Corp. v. Florida*, as well as the language in *McKesson Corp.* support the requirement of a post-deprivation remedy in not only cases of tax laws violating the Constitution, but also any unlawful taxes. States have sought to limit the reach of *McKesson* by alleging that the judicial remedy must only be provided for taxes that are found to be unconstitutional, yet this limit conflicts with prior decisions of this Court and deprives taxpayers of their constitutional right to a post-deprivation judicial remedy through which they can contest their disputed taxes.

This Court specifically cited to *Ward* which dealt with a violation of *federal* law, not an unconstitutional law: "To say that the county could collect these unlawful taxes by coercive means and not incur any obligation to pay them back is nothing short of saying that it could take or appropriate the property of these Indian allottees arbitrarily and without due process of law." *McKesson Corp. v. Florida*, 496 U.S. 18, 33 (1990) (citing *Ward v. Board of County Com'rs of Love County*, 253 U.S. 17, 24 (1920)). This Court also refe-

renced *Carpenter v. Shaw*: ". . . a denial by a state court of a recovery of taxes exacted in violation of the laws or Constitution of the United States by compulsion is itself in contravention of the Fourteenth Amendment." *Carpenter v. Shaw*, 280 US 363, 369 (1930) (emphasis added). The references by this Court to past cases, as well as the language used by this Court in *McKesson Corp. v. Florida*,[2] make it clear that the Due Process right to backward-looking relief does not hinge on a constitutional violation, but rather an unlawful collection of taxes. Thus, Kentucky's failure to provide meaningful backward looking relief for petitioners as required by *McKesson* violated their Due Process rights.

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[2] "Because exaction of a tax constitutes a deprivation of property, the State must provide procedural safeguards against unlawful exactions in order to satisfy the commands of the Due Process Clause." *McKesson Corp. v. Florida*, 496 U.S. 18, 36 (1990).

CONCLUSION

For the reasons stated above, and for the reasons identified by Petitioner, this Court should grant the Petition for a Writ of Certiorari.

Respectfully submitted,

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